

**DEPARTMENT OF STATE REVENUE
LETTER OF FINDINGS NUMBER: 03-0317
Individual Income Tax
For the Years 1997-2001**

NOTICE: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication. It shall remain in effect until the date it is superseded or deleted by the publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUES

I. Tax Administration - Best information available

Authority: Ind. Code § 6-3-1-3.5; Ind. Code § 6-8.1-5-1; Ind. Code § 6-8.1-5-2; Ind. Code § 6-8.1-5-4.

Taxpayer protests the assessment of adjusted gross income tax, based on the Department's determination of its gross receipts.

II. Tax Administration - Penalty

Authority: Ind. Code § 6-8.1-10-2.1; 45 IAC 15-11-2(b).

Taxpayer protests the imposition of the ten percent (10%) negligence penalty.

STATEMENT OF FACTS

Taxpayers are a married couple whose primary source of income is derived from sales of rental booths and food sales during festivals held during holidays. During the years in question, Taxpayers filed federal and state income tax returns. As a result of Department audit, Taxpayers' gross sales were increased substantially, with an allowance made for expenses associated with food sales. Taxpayer protested the assessment, both for the amount and the timeliness of the assessment.

I. Tax Administration-Best information available

DISCUSSION

Taxpayers argue that the assessment of additional income was too high. In addition, Taxpayers note that they filed federal income tax returns for the years in question, and their state income tax returns matched their federal income tax returns. While federal adjusted gross income is the starting point for determining an individual's Indiana income tax liability per Ind. Code § 6-3-1-3.5(a), the Department's audit is presumed to be correct. Ind. Code 6-8.1-5-1(b).

Under Ind. Code § 6-8.1-5-4, a taxpayer is required to keep records including “all source documents necessary to determine the tax, including invoices, register tapes, receipts, and canceled checks.” Here, Taxpayer has submitted handwritten records for the past several years. While these records provide a modicum of effort with respect to record keeping, a third-party record of Taxpayers’ activities—e.g., bank account records showing deposits and withdrawals or some other similar records—would be necessary to verify Taxpayers’ records under these circumstances. However, Taxpayers have provided sufficient information to conclude that several deductions listed on their federal income tax return in arriving at adjusted gross income were not considered by the auditor, and accordingly those deductions should be permitted.

Taxpayers have further protested the assessment of income tax for the years from 1997 to 1999, noting that the years are beyond the normal three-year statute of limitations provided by Ind. Code § 6-8.1-5-2(a). In the case of underreporting one’s income by at least twenty-five percent, the statute of limitations is extended to six years. Ind. Code § 6-8.1-5-2(b). Here the amount of underreported income can only be determined after further review, and accordingly is either sustained or denied based on that determination.

FINDING

Taxpayers’ protest is sustained to the extent of the excess deduction and to the extent that Taxpayers’ income was not underreported by at least 25% for the years from 1997 to 1999. Taxpayers’ protest is otherwise denied.

II. Tax Administration - Penalty

DISCUSSION

Penalty waiver is permitted if the taxpayer shows that the failure to pay the full amount of the tax was due to reasonable cause and not due to willful neglect. Ind. Code § 6-8.1-10-2.1. The Indiana Administrative Code further provides in 45 IAC 15-11-2:

(b) "Negligence" on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence. Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer.

(c) The department shall waive the negligence penalty imposed under IC 6-8.1-10-1 if the taxpayer affirmatively establishes that the failure to file a return, pay the full amount of tax due, timely remit tax held in trust, or pay a deficiency was due to reasonable cause and not due to negligence. In order to establish reasonable cause, the taxpayer must demonstrate that it exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving

rise to the penalty imposed under this section. Factors which may be considered in determining reasonable cause include, but are not limited to:

- (1) the nature of the tax involved;
- (2) judicial precedents set by Indiana courts;
- (3) judicial precedents established in jurisdictions outside Indiana;
- (4) published department instructions, information bulletins, letters of findings, rulings, letters of advice, etc.;
- (5) previous audits or letters of findings concerning the issue and taxpayer involved in the penalty assessment.

Reasonable cause is a fact sensitive question and thus will be dealt with according to the particular facts and circumstances of each case.

A basic duty of care exists for all taxpayers, from individuals of the most modest means to the largest corporations. That duty is one of knowledge of tax laws, knowledge of payment and filing deadlines, and record keeping of one's own business and personal affairs sufficient to retrace their prior financial transactions as necessary for a reasonable period of time. To impute less of a duty is to allow for carelessness or even intentional ignorance to be a defense-something that no effective legal system can permit. If a taxpayer is not certain of the scope of that duty, professional advice and even the occasional question to the Department is available. Taxpayer's actions did not meet the standard necessary to justify penalty waiver.

FINDING

Taxpayer's protest is denied.